

***United States Court of Appeals
for the Second Circuit***



AMICUS BRIEF

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75-2542

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

CHRIS-CRAFT INDUSTRIES, INC.,

Plaintiff-Appellant-
Cross-Appellee,

v.

PIPER AIRCRAFT CORPORATION, HOWARD PIPER,
THOMAS F. PIPER, WILLIAM T. PIPER, JR., BANGOR
PUNTA CORPORATION, NICOLAS M. SALGO, DAVID W.
WALLACE and THE FIRST BOSTON CORPORATION,

Defendants-Appellees-
Cross-Appellants.

Appeal from a Judgment of the United States
District Court for the Southern District of New York

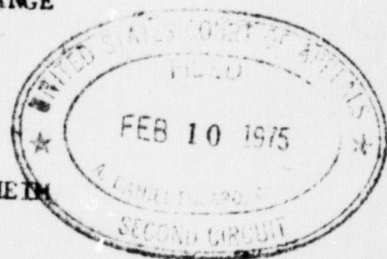
MEMORANDUM OF THE SECURITIES AND EXCHANGE
COMMISSION, AMICUS CURIAE

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UNITED STATES COURT OF APPEALS
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CHRIS-CRAFT INDUSTRIES, INC., :

Plaintiff-Appellant- :
Cross-Appellee, :

v. :

Docket No. 75-2542

PIPER AIRCRAFT CORPORATION, HOWARD :
PIPER, THOMAS F. PIPER, WILLIAM T. :
PIPER, JR., BANGOR PUNTA CORPORATION, :
NICHOLAS M. SALGO, DAVID W. WALLACE :
and THE FIRST BOSTON CORPORATION, :

Defendants-Appellees- :
Cross-Appellants. :

MEMORANDUM OF THE SECURITIES AND
EXCHANGE COMMISSION,
AMICUS CURIAE

This is an appeal from a judgment of the United States District Court for the Southern District of New York granting certain damages and injunctive relief, 1/ purportedly in accordance with instructions from this Court on a previous appeal. 2/ The Securities and Exchange Commission submits this memorandum, amicus curiae, in support of reversal on the ground that the relief and damages granted below are insufficient.

1/ Chris-Craft Industries, Inc. v. Piper Aircraft Corp., 384 F.Supp. 507 (S.D.N.Y., 1974).

2/ Chris-Craft Industries, Inc. v. Piper Aircraft Corp., 480 F.Supp. 341 (C.A. 2, 1973).

The Interest of the Securities and Exchange
Commission in this Case

In its appeal, Chris-Craft argues that the judgment of the District Court on remand fails to implement the prior decision of this Court directing both an award of damages in favor of Chris-Craft and the issuance of an injunction against the voting of certain shares of Piper Aircraft Corporation ("Piper") owned by Bangor Punta Corporation ("Bangor Punta") and acquired by Bangor Punta in violation of the Securities Exchange Act of 1934.

The Commission believes that the judgment of the District Court frustrates both the prior decisions of this Court in the instant case 3/ and the policies of investor protection and fair dealing embodied in the federal securities laws. In a suit arising out of certain of the same unlawful conduct on the part of the defendants in this case the Commission sought injunctive relief against Bangor Punta in order, inter alia, to make it clear to contestants in corporate take-over battles that they could not violate the law with

3/ Id.; and Chris-Craft Industries, Inc. v. Bangor Punta Corp., 426 F.2d 569 (C.A. 2, 1970) (en banc).

impunity. 4/ Notwithstanding the violations of Section 10(b) and 14(e) of the Securities Exchange Act of 1934 which form the basis for this case -- and notwithstanding the defendants' earlier violations of Section 5 of the Securities Act of 1933 5/ -- the District Court denied the injunctive relief sought by the Commission. On an appeal to this Court, consolidated with the prior appeal in the present case, the denial of the injunctive relief sought by the Commission was upheld by a divided court. In denying injunctive relief to the Commission, Judge Gurfein, speaking for the majority, indicated that the "didactic" effect of the damages awarded to Chris-Craft would have at least as salutary an effect on the conduct of take-over combatants. 480 F.2d at 395. In his concurring opinion, Judge Mansfield agreed that "[t]he relief granted

4/ Securities and Exchange Commission v. Bangor Punta Corp., 331 F.Supp. 1154 (S.D.N.Y., 1971), aff'd. in part and rev'd. in part, 480 F.2d 341 (C.A. 2, 1973), rehearing denied, 480 F.2d 407 (C.A. 2, 1973), certiorari denied, 414 U.S. 924 (1973).

5/ Bangor Punta consented to the entry of an injunction against offers of securities in violation of Section 5 of the Securities Act (15 U.S.C. §77e) in the District Court for the District of Columbia, on May 26, 1969.

[to Chris-Craft] is bitter medicine which will be far more effective than a blanket injunction in deterring infraction of the law." Id. at 406-07. Having been denied the relief which it believed necessary to serve the public interest, the Commission respectfully urges this Court to require an award of damages and appropriate injunctive relief that will preclude the violators from enjoying the "fruits" of the illegally acquired Piper shares. Id. at 380.

Although the Commission has not previously taken any position on the question of damages in this case, it believes that the calculation of damages by the District Court is internally inconsistent and avoids the impact of this Court's decision -- with which the District Court apparently disagrees. 6/ The Commission is also of the view that the injunctive relief fashioned by the District Court may subvert the type of rescission offer which this Court required Bangor Punta to make to certain former shareholders of Piper. 7/

6/ Chris-Craft Industries, Inc. v. Piper Aircraft Corp., 384 F.Supp. 507, 513-514 (S.D.N.Y., 1974).

7/ Securities and Exchange Commission v. Bangor Punta Corp., 480 F.2d 341, 390-92 (C.A. 2, 1973).

DISCUSSION

- I. THE INJUNCTIVE RELIEF PROVIDED BELOW
FAILS TO DENY BANGOR PUNTA THE FRUITS
OF ITS VIOLATIONS OR TO SERVE THE PUBLIC
INTEREST.

In directing the entry of an injunction barring the voting of the Piper shares acquired by Bangor Punta in violation of the Securities Exchange Act of 1934, this Court recognized the necessity to deny Bangor Punta the "fruits of its violations." 480 F.2d at 380. As contended in Appellant's brief, (pp. 51-54), the injunctive relief provided by the District Court appears to have failed to effect such a denial, and, in fact, appears to perpetuate Bangor Punta's dominance over Piper by (i) producing a stalemate in the Board of Directors, (ii) providing Bangor Punta with a veto over all significant corporate action, and (iii) sanctioning whatever control Bangor Punta has exercised in the selection of Piper's officers. As Chris-Craft points out, with Bangor Punta assured of absolute control at the end of five years, the primary loyalty of Piper's officers and employees can be expected to run to Bangor Punta.

Accordingly, it appears that the District Court's judgment fails to achieve the ends sought by this Court's decision and fails to effectuate the public interest to be served by the injunctive relief. Nevertheless, it is clear that the present case is unique in that the shares which are to be enjoined from voting are the very shares which hold the balance of power over Piper. This situation -- and Chris-Craft's apparent continued interest in achieving control of Piper -- were not foreseen when this case was last before this Court. 8/

The Commission vigorously opposes the form of injunctive relief awarded by the District Court on an additional ground: the remaining public shareholders of Piper -- some 1,400 persons holding over 78,000 shares -- will be effectively

8/ In awarding damages to Chris-Craft rather than forcing divestiture of Bangor Punta's unlawfully acquired shares, this Court assumed that the battle for control of Piper was at an end. 480 F.2d at 379. The injunctive relief directed by this Court appears to have rekindled Chris-Craft's interest in seeking control of Piper. With the prospect of the 231,002 shares of Piper enjoined from voting, Chris-Craft purchased additional Piper shares which would give it over 50% of the outstanding shares presumed to have voting rights.

"locked-in" for another five years 9/ during which Piper may drift, without decisive leadership or direction. With Piper under the direct control of either Chris-Craft or Bangor Punta, these shareholders might improve their lot. Furthermore, the Commission is concerned that the present injunction may render futile the rescission offer which Bangor Punta is required to make: it is unrealistic to assume that persons who surrendered Piper stock for Bangor Punta securities will exercise their rescission right if all they stand to acquire is the likelihood of being merged back into Bangor Punta at a possibly depressed price five years later. 10/

9/ The present distribution of stock supplies little incentive for purchaser interest. Under the present injunction, neither Chris-Craft (which now has more than 50% of the stock not subject to the injunction) nor Bangor Punta (which has more than 50% of the outstanding stock) would appear to have any incentive to purchase additional shares of Piper stock. Particularly in view of the limited amount of stock available for a "float," Piper stock must be regarded as a somewhat illiquid investment.

10/ The lack of market liquidity and purchaser interest referred to in note 9, supra, could well depress the market price.

While the Commission believes that the form of injunctive relief proposed by Chris-Craft would constitute a particularly effective deterrent to securities laws violations in connection with contests for corporate control, the issuance of such an injunction would not significantly alter the posture of Piper's remaining shareholders. If this Court shares the concern of the District Court that subjecting Bangor Punta's majority equity interest in Piper to the control of Chris-Craft is too harsh a penalty, perhaps this unique situation calls for a unique solution. As in J. I. Case Co. v. Borak, 377 U.S. 426 (1964), so here

" . . . under the circumstances . . . it is necessary to provide such remedies as are necessary to make effective the Congressional purposes."

Id. at 433.

A possible solution would, in effect, treat the 231,002 shares illegally acquired by Bangor Punta as though they were held in a voting trust: during the period of the injunction Bangor Punta would be required to vote the shares

in proportion to and in the manner that the publicly held shares are voted. 11/ The Commission recognizes that the issuance of a mandatory injunction requiring Bangor Punta to vote its shares in this manner might probably have the effect of reopening the contest for control of Piper. 12/ It may be, however, that a proxy contest in which the public shareholders of Piper have the right to weigh the relative merits of Chris-Craft's and Bangor Punta's plans for the future operation of Piper is the appropriate arena in which this battle should be waged.

Both Chris-Craft and Bangor Punta accepted the risk that one of them would end up with a sizeable minority

11/ Specifically, the Commission suggests consideration of the issuance of a mandatory injunction against Bangor Punta requiring that, for a period of at least five years, the 231,002 shares of Piper stock unlawfully acquired (less such number of shares as may be disposed of pursuant to the rescission offer) be voted in proportion to the votes of the 89,374 shares publicly held at September 5, 1969 (plus such number of Piper shares as may be disposed of pursuant to the rescission offer). Shares acquired by either Chris-Craft or Bangor Punta after September 5, 1969 would be included in the determination of the voting of the shares -- thus, the 10,805 shares of Piper stock subsequently acquired by Chris-Craft would partially influence the shares voted under the injunction.

12/ Either Chris-Craft or Bangor Punta could acquire an absolute majority of the voting rights to Piper's stock even during the period of the injunction.

position by continuing their acquisitions of, and exchange offers for, Piper stock up to the point of Bangor Punta's unlawful conduct. Chris-Craft has suffered because of the unlawful means utilized by Bangor Punta to acquire control -- means which were also available to, but rejected by, Chris-Craft. The proposed solution would simply return the parties -- and the public -- to approximately the situation which would have existed absent Bangor Punta's unlawful conduct.

II. THE DETERMINATION OF DAMAGES BY
THE DISTRICT COURT WAS INCORRECT

In remanding this case to the District Court, this Court directed that Chris-Craft be awarded damages measured by "the reduction in the appraisal value of CCI's Piper holdings attributable to BPC's taking a majority position and reducing CCI to a minority position, and thus being able to compel a merger at any time." 480 F.2d at 380.

By directing that damages be based upon the reduction in the "appraisal value," the Commission believes this Court intended to go beyond the traditional measure of damages provided to purchasers under the federal securities laws. Whereas the traditional measure is based upon an investor's cost, 13/ this Court apparently recognized that the injury for which Chris-Craft was to be compensated occurred subsequent to the times at which Chris-Craft

13/ See, e.g., Section 11 and 12 of the Securities Act of 1933, 15 U.S.C. Sections 77k and 77l, both of which make the injured investor whole through rescission or reimbursement of out-of-pocket losses. These statutory remedies have been extended to implied causes of action arising under the federal securities laws. See, e.g., Chasins v. Smith, Barney & Co., 438 F.2d 1167 (C.A. 2, 1970); Esplin v. Hirschi, 402 F.2d 94 (C.A. 10, 1968); Janigan v. Taylor, 344 F.2d 781 (C.A. 1, 1965).

Application of the traditional measure of damages to the present situation would suggest that Chris-Craft should at the very least receive the difference between its cost (averaging \$64 per share) and the value of its holdings at such time after Bangor Punta acquired control of Piper as Chris-Craft could have disposed of its holdings. Plaintiff's witness, Wahrsager, indicated
(Footnote Continued)

acquired its interest and that using cost as a starting point might unfairly penalize Chris-Craft. The injury was to the value of its accumulated holdings -- a value presumably in excess of its cost, since Chris-Craft's earlier-acquired shares were purchased at a lower cost and the amount of premium attributable to its holdings would increase as it approached control.

Although the District Court admits to having struggled with the meaning to be given the term "appraisal value" 14/ the theory which it adopted appears to agree with this rationale. The opinion appears to conclude that the measure of damages is to be the difference between (i) the value of Chris-Craft's holdings prior to the date that Bangor Punta's unlawful acquisitions put the latter in

13/ (footnote continued)

Chris-Craft would have received only \$33 per share on disposition (if disposition were effected by a public offering in November 1969) (EV 821), resulting in damages of \$31 per share; defendants' witness, Gant, estimated higher proceeds of approximately \$42 per share (EV 1236), resulting in damages of at least \$22 per share.

14/ One possible interpretation considered by the District Court was to treat the proceeding as though statutory appraisal rights were being exercised by a dissenting shareholder. The District Court rejected this approach, arguing that the "inherent" or underlying value of Chris-Craft's holding of Piper shares was the same before and after September 5, 1969, when Bangor Punta achieved its absolute majority. Although rejection of this approach would be appropriate if Chris-Craft's shares were to be valued solely at their aliquot interest in Piper's underlying assets, the Commission believes that an actual statutory appraisal proceeding in the dissenters' right context should have valued the shares at an amount at least equal to the alleged value of Bangor Punta's exchange offer.

control of Piper and (ii) the value of Chris-Craft's holdings after such control was achieved. In applying this measure of damages, the District Court began by measuring the value of Chris-Craft's holdings of Piper stock as though it held a hypothetical 42% to 37% lead in the contest for control. Once the appraisal value of that plurality position was determined, the District Court proposed to deduct the value of Chris-Craft's holding at September 5, 1969 -- when Bangor Punta had achieved a 51% to 42% majority.

The Commission agrees that the theory purportedly adopted by the District Court provides a proper measure of the damages which Chris-Craft suffered. The principal difficulty with the judgment below is that while purporting to adopt an appropriate theory, the District Court erroneously limited the scope of its inquiry. 15/ Having selected a theory for measuring damages, the Court reviewed the evidence on the value of Chris-Craft's holdings of Piper stock, using a 100 share trading unit

15/ In addition, it does not appear that the District Court arrived at a fair market value, since the actual market price was ignored. 384 F. Supp. 507, 515. The value arrived at by the District Court necessarily assumed that reasonable businessmen would engage in a contest in which they would offer to pay 50% to 75% more than the value of what they would acquire. Such an assumption appears unreasonable on the facts of this case.

to determine the fair market value of Piper stock, and found it to be \$48 per share. 16/ The District Court applied a 5% premium to this value to reflect Chris-Craft's lead in the battle for control of Piper and awarded damages of \$2.40 per share to Chris-Craft.

The District Court ended its inquiry at that point, without examining whether the value of Chris-Craft's holdings declined below "fair market value" after Bangor Punta achieved control. Despite the testimony not only of plaintiff's experts but also of some of defendant's experts, the District Court failed to recognize any reduction in the value of Chris-Craft's holdings by reason of Bangor Punta having achieved control. At best, the decision of the District Court is based on an incomplete calculation as a result of its assumption that the inherent value of Chris-Craft's holdings of Piper stock was unchanged. Gant, the defense witness whose testimony provided the basis for the 5% premium value applied by the District Court also testified that, once Bangor Punta achieved control, Chris-Craft

16/ In a footnote in Chris-Craft's brief (p. 27) it is contended that the \$48 per share market value determined by the District Court resulted from the use of incorrect figures and that the correct average was \$54 per share.

would have realized less than the market price applicable to a 100-share trading unit. In a hypothetical underwritten public offering on September 5, 1969, Gant estimated net proceeds of \$41.60 to \$43.50 per share 17/ -- a discount of over 10% from the market value determined by the court. In the case of a hypothetical private sale on September 5, 1969, Gant estimated that the discount would be 25% to 30% below market. 18/ This discount would result from the limited market for resale, the necessity of registration prior to resale and the expense of the selling effort necessary to accomplish a resale. Assuming, arguendo, that the \$48 per share figure determined by the District Court represented fair market value for Piper stock, the minimum damages appropriate under this theory would be 30% -- the difference between a 5% premium and a 25% discount -- of the market value: resulting in damages of \$14.40 per share rather than the \$2.40 awarded by the District Court.

In computing the foregoing alternative figures which would result in alternative awards of damages to Chris-Craft the Commission has uncritically utilized valuations included in the record. The Commission expresses

17/ 2823A.

18/ 3831A. It is interesting to note that Gant's estimate of a 40% differential (10% premium and a 30% discount), if applied to Chris-Craft's actual cost of \$64 per share, would indicate a post-September 5 value of approximately \$38 per share (damages of \$26.00 per share) which approximates the average of Gant's and Wahrsager's estimates. See note 13, supra.

no view on whether the record is sufficient to award damages based on any of the calculations suggested, particularly since each witness appears to have proceeded on a different theory of valuation. If the present record is not sufficient, the Commission believes the case should be remanded with explicit instructions to the District Court on the theory to be applied. 19/

CONCLUSION

The decision of the District Court is inconsistent with the ends sought by this Court in directing the entry of an award of damages and injunctive relief. The didactic effect of the judgment below is that those who violate the securities laws may be rewarded while those who do not may be penalized for obeying the law. The bitter medicine sought to be administered by this Court is discovered to be only a placebo which results in Bangor

19/ The Commission believes such instructions should also indicate the effect, if any, to be given to the possible mitigation of Chris-Craft's damages, as a result of the injunctive relief awarded. Assuming, arguendo, that injunctive relief in the form suggested by Chris-Craft or by the Commission would partially restore the loss in the appraisal value of Chris-Craft's Piper holdings, it would not eliminate all damages since Chris-Craft has had considerable interest expense in carrying its investment during the pendency of this case.

Punta's having saved approximately \$11,000.000. 20/
The Commission believes the public interest requires
reversal of the District Court.

Respectfully submitted,

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20/ The damages awarded by the District Court actually result in a savings rather than a loss or penalty to Bangor Punta, which has avoided, and in its 1973 annual report wrote off a liability of approximately \$13,000.000 to the Piper family based on Bangor Punta's alleged failure to possess control of Piper because of the injunction. Having "lost" the battle, Bangor Punta gains an unexpected windfall and enjoys continued domination of Piper's affairs.